State of Colorado

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Honorable Bill Owens
Governor of Colorado
136 State Capitol Building
Denver, Colorado 80203

Honorable Senator Abel Tapia
Chair, Joint Budget Committee
Colorado General Assembly
200 East 14th Avenue
Denver, Colorado 80203

Dear Governor Owens and Senator Tapia:

In accordance with the Total Compensation Reform Act, the enclosed 2006-07 Annual Compensation Report indicates $93 million is needed to reach prevailing market compensation for next fiscal year[1] as shown in the following table. However, our strategic plan would indicate a need of an additional $70.2 million to keep salaries competitive and to continue to incrementally increase employer contributions for group benefits toward prevailing market practices so that we do not risk falling irreparably behind the market.

FY 2006-07 ANNUAL COMPENSATION SURVEY FINDINGS AND ESTIMATED COST
(Including associated PERA and Medicare costs)

Type of Compensation	Compensation At 75% HLD	Prevailing Market Compensation
Occupational Salary Range Adjustments (2.8%)	$31,971,353	$31,971,353
Performance Base-Pay (0.84%)	$9,541,594	$9,541,594
Performance Non-Base Pay (1.25%)	$14,211,170	$14,211,170
HLD Contributions[2]	$14,463,214	$37,317,871
Total Compensation Package New Dollars	$70,187,331	$93,041,988

[1] This estimated cost is for OSPB agencies, which excludes Higher Education Institutions, Department of Law, Treasury, Department of State, Judicial, and the General Assembly.
[2] The Department's five-year strategic plan is to achieve prevailing cash contribution levels for health, life, and dental benefits, to reach a meaningful performance award amount that corresponds with the market, and maintain salary structure adjustments in order to ensure the State is able to recruit and retain a competent workforce. This plan required benefit cash contribution levels at 75% of prevailing in FY 2006-07.

Salary data indicates the need for a statewide average range adjustment of 2.8%. The salary adjustment would maintain the State's competitive pay ranges and assure employees are being paid comparably to the private sector.[3] The specific salary adjustment indicated for each occupational group is shown in the table below.

Occupational Group	Average Market Midpoint Increase	Total State Employees
ENFORCEMENT AND PROTECTIVE SERVICES* (EPS)	3.2%	5307
TROOPERS	5.1%	666
FINANCIAL SERVICES (FS)	1.1%	1797
HEALTH CARE SERVICES (HCS) [and Medical**(MED)]	4.2%	3463
LABOR/TRADES/CRAFTS (LTC)	1.6%	5592
ADMINISTRATIVE SUPPORT AND RELATED (ASR)	2.4%	5014
PROFESSIONAL SERVICES (PS) [and Teachers* (T)]	2.2%	8447
PHYSICAL SCIENCES AND ENGINEERING (PSE)	1.6%	1970

* Per C.R.S. 24-50-104(1)(a)(III)(A), Trooper's market (top three highest-paid large jurisdictions) shows a 5.1% structure movement and a 6.0% actual pay difference between the State and this market, with SB 03-273 applied. While the 5.1% structure movement would be applied for the range adjustment for Troopers, the 6.0% would be used for Troopers' salary adjustments if the Annual Compensation Survey findings were implemented.

**Due to the lack of statistically valid survey data for the Teacher and Medical occupational groups, the PS occupational group increase is used for Teacher and the HCS occupational group for Medical.

The survey data also indicates the need to allocate 0.84% of total payroll for base building performance awards and 1.25% for non-base building performance awards. Under the former step system, the State budgeted approximately 2.2% to ensure that employees could progress through their pay ranges. Despite legislative intent for performance pay to be cost neutral in relation to the former step system, appropriations for performance-based pay over the past four years were limited to 1.1% for FY 2002-03, 0% for FY 2003-04, 1.1% for FY 2004-05, and 0% for FY 2005-06. The survey indicates that the State lags the market in its total salary compensation due to the lack of funding and our exclusion of a non-base performance pay component. In addition, it must be noted that if the survey findings related to performance pay were to be implemented, less than half of the total appropriations for performance pay would be base building, and although the total amount of funding dedicated to performance pay would be higher than it has been historically, the portion that is base building would be materially consistent with historical appropriations for performance pay, in the fiscal years in which this component of total compensation has been funded. It is my long-term goal to allocate a sufficient amount of budget in order to assure that state employees have a real opportunity to move through their pay ranges and to receive meaningful performance pay. This is consistent with the Department's five-year strategic plan to reach a meaningful total compensation package for our employees.

Included in the survey data indicating a 2.8% increase to the pay range structure, and consistent with historical practice, the Department conducted a detailed analysis of individual class pay ranges versus the labor market pay ranges because individual class pay ranges may move differently than the overall occupational group movement. We found that several classes need adjustment in order to remain competitive with the market. For example, Nurse classes need to be adjusted upward in response to labor market shortages in this occupation.

[3] Employees rated "Needs Improvement" will be prohibited from receiving salary adjustments.

Additionally, survey data indicates a need to shift the State's minimum rates in order to have ranges comparable to the survey market. This will ensure all ranges are at least two percent closer to the market hiring rates. By closely monitoring the market's hiring practice and modifying the State's hiring rate policy, the intent is to create competitive hiring compensation that will help with statewide recruitment.

Turning to the State's contribution to group benefit plans, additional funding is needed to continue bringing the employer's contribution closer to market. These new dollars will help address the critical issue of recent annual double-digit increases in health care premiums and bring our health care contributions closer to prevailing practice. For group insurance contributions, the State continues to be below the market. One of the goals in our five-year strategic plan is to reach prevailing employer contribution levels and to allow state employees the flexibility of choosing the compensation package that best meets their needs. The Department's total compensation strategy is to incrementally increase the employer's contribution. The State's contribution was an average of 49% of employer contribution levels, which increased to an average of 56% of market during FY 2004-2005 (January 2005). This past year, the General Assembly funded our recommendation that allowed us to reach an average of 66%[4] of the prevailing employer contribution as of July 1, 2005. The plan outlined an increase for FY 2006-07 to allow the State to close this critical gap by building on last two year's progress and take the State to an average of 75% of the prevailing employer contribution levels. It is important to note that the employer contribution level is only one aspect that must be measured to determine if the State's benefits are prevailing on an overall basis. When items such as co-pays, deductibles, and out-of-pocket maximums are taken into consideration, the State is below market levels in these areas as well. The Department is planning to close these gaps through planned design improvements. The following table shows the increase in state contributions for FY 2006-07 to achieve the goals in the Department's five-year strategic plan.

	Health		**Dental**		**Life**	
	75% Market	State Current $	75% Market	State Current $	75% Market	State Current $
Employee	$244.00	$190.20	$19.00	$14.90	$8.00	$4.68
Employee + Spouse	$413.00	$333.96	$28.00	$18.38		
Employee + Child(ren)	$381.00	$322.32	$32.00	$19.78		
Employee + Spouse + Child(ren)	$567.00	$460.27	$41.00	$23.12		

The annual compensation survey findings indicate that a total additional cost of $70.2 to $93 million is needed for the State to match prevailing salary practices and to narrow the gap with respect to benefits practices for both its classified and non-classified appropriated positions. Unfortunately, the June 2005 fiscal forecast by the Office of State Planning and Budgeting estimates that a General Fund reduction of $207.8 million is necessary in FY 2006-07 based upon current law. As a result of

[4] This figure is higher than the 59.5% projected for July 1, 2005, primarily due to the fact that the projected trend used in last year's report was higher than the actual premium rate increases in the market and, to a lesser degree, it also reflects a cost containment technique in the market of shifting some of the premium costs to employees.

this disappointing forecast, I cannot, at this time, make a recommendation to adjust salaries by the prevailing market findings as indicated by our salary survey or to increase the HLD contribution levels to 75% of the prevailing practice in the private sector. However, I intend to discuss this critical issue with the Joint Budget Committee and the entire General Assembly as soon as they reconvene in January 2006.

The current fiscal conditions and the budget constraints of the past few years have already taken a toll on the state's ability to attract and retain a competent workforce. Additionally, approximately 30% of our current workforce will be retirement eligible within the next 5 years. As a result, it is imperative that the State attempt to meet its obligation to offer a competitive total compensation package to its current and prospective employees.

Please visit the following site for FY 2006-07 annual compensation survey findings **http://www.colorado.gov/dpa/dhr/comp/pay.htm**.

Sincerely,

Jeffrey M Wells

Jeffrey M. Wells
Executive Director

cc: State Legislators, Cabinet Members and Higher Education Presidents.